**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**Washington, D.C. 20554**

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| In the Matter of | ) | |
| | ) | |
| Federal-State Joint Board on Universal Service | ) | CC Docket No. 96-45 |
| | ) | |
| 1998 Biennial Review – Streamline Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms | ) | CC Docket No. 98-171 |
| | ) | |
| Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans with Disabilities Act of 1990 | ) | CC Docket No. 90-571 |
| | ) | |
| Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Size | ) | CC Docket No. 92-237<br>NSD File No. L-00-72 |
| | ) | |
| Numbering Resource Optimization | ) | CC Docket No. 99-200 |
| | ) | |
| Telephone Numbering Portability | ) | CC Docket No. 95-116 |
| | ) | |
| Truth-in-Billing and Billing Format | ) | CC Docket No. 98-170 |

# NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION INITIAL COMMENTS


NATIONAL TELECOMMUNICATIONS
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**SUMMARY**

In its comments, NTCA offers its evaluation of the Commission's staff analysis of proposed universal service contribution methodologies. Due to the complexity of the staff study model and the hundreds of underlying assumptions, NTCA chose several itemized estimates in the staff study it believed were highly significant to compare the three proposed mechanisms.

The two-connection-based and the telephone number-based methodologies proposed by the Commission each contain flaws and have inherent conflicts with Section 254(d) and 2(b) of the Act that requires carriers to contribution to USF on an equitable and non-discriminatory basis and prohibits an assessment on intrastate revenues to support the interstate universal service fund.

A revenue-based mechanism is economically efficient. Assessments based on retail revenues are self-correcting and adjust instantaneously with changes in consumer spending. The problems with the current revenue-based mechanism are the result of regulatory arbitrage, such as the exemption of cable, wireless and satellite communications from the same universal service obligations as ILECs. The elimination of regulatory arbitrage and application of the revenue-based system evenly to all interstate and international revenues regardless of technology used will ensure sufficient universal service funding and the long-term viability of the fund.

Nothing contained in the staff study or previous rulings has proved that a connection or number-based system is superior to the revenue-based system. To change to an economically and administratively unproven and legally questionable methodology would not be in the public interest.

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**NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION**
**INITIAL COMMENTS**

The National Telecommunications Cooperative Association (NTCA)[1] hereby files its initial comments in response to the Federal Communications Commission's (Commission or FCC) Public Notice in the above-captioned proceeding seeking public

[1] NTCA is the premier industry association representing rural telecommunications providers. Established in 1954 by eight rural telephone companies, today NTCA represents 560 rural rate-of-return regulated incumbent local exchange carriers (ILECs). All of its members are full service local exchange carriers and many members provide wireless, cable, Internet, satellite and long distance services to their communities. Each member is a "rural telephone company" as defined in the Communications Act of 1934, as amended (Act). NTCA members are dedicated to providing competitive modern telecommunications services and ensuring the economic future of their rural communities.

comment on an FCC staff study regarding alternative universal service contribution methodologies.[2]

NTCA's ability to comment on the merits of each proposed funding mechanism is limited due to several factors, such as the extreme complexity of the model used by the FCC to evaluate the contribution mechanisms, the hundreds of assumptions used as the basis of the model, and the outdated format in which the staff study was presented. Second, models and predictions are by their very nature incorrect.

Regardless of which contribution assessment the Commission ultimately chooses the agency is required by law to meet certain requirements. Section 254(d) of the Act states that "every telecommunications carrier that provides interstate telecommunications service shall contribute on an equitable and non-discriminatory basis" to universal service. Furthermore, the United States Court of Appeals for 5th Circuit has determined that the Commission is prohibited under section 2(b) from assessing intrastate revenues to support the interstate universal service fund.[3]

## I. ASSESSMENT OF METHODOLOGIES USING STAFF STUDY RESULTS

The staff study used a model to estimate the potential assessment levels and other information by which commenters may evaluate the proposed mechanisms. To justify

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[2] *In the Matter of Federal-State Board on Universal Service*, CC Docket No. 96-45, *1998 Biennial Regulatory Review – Streamline Contributor Reporting Requirements Associated with the Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms*, CC Docket No. 98-171, *Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans with Disabilities Act of 1990*, CC Docket No. 90-571, *Administration with the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size*, CC Docket No. 92-237, NSD File No. L-00-72, *Numbering Resource Optimization*, CC Docket No. 99-200, *Telephone Number Portability*, CC Docket No. 95-116, *Truth-in-Billing and Billing Format*, CC Docket No. 98-170, FCC 03-31, Public Notice Seeking Comment on Staff Study Regarding Alternative Contribution Methodologies. (rel. Feb.26, 2003).

[3] *Texas Office of Public Utility Counsel v. FCC,* 183 F.3d 393, 448 (5th Cir. 1999).

implementing a new universal service contribution mechanism the Commission must make a positive finding that an alternative mechanism is clearly superior to the revenue-based one. In the absence of such a finding, the Commission should not make change for change sake alone.

Assuming the underlying assumptions and modeling used to create the estimates in the staff study are correct, and using the current revenue based proposal as the baseline, NTCA evaluated the proposed mechanisms on the four items it deemed most significant: share of contributions by industry segment; average monthly pass-through charge per household; sample contributions by industry segment per month; and the percentage breakdown of the universal service fund burden met by residential/business assessments.[4]

### A. Proposal #1 – Connection Based Methodology

Upon first look the first connection-based proposal appears to be comparable to the revenue based proposal in many ways. Its average monthly pass-through charge per household estimated at $2.34, just four cents below the revenue based estimate. The percentage of the fund met from residential/business assessments is identical at 42% to 58% respectively to the revenue-based mechanism.

As with the telephone line mechanism proposal, the faults of this method begin to show when you look at the breakdown of the estimated monthly fee for this methodology per market segment. Specifically, the contributions by industry segments do not meet the equitable and non-discriminatory requirements of the 1996 Telecom Act. While the staff study predicts the share of industry segment contributions to be 22% by IXCs, 45% for

ILECs and 31% for CMRS carriers, the break down of actual contributions per industry segment do not seem to reflect this percentage. The $2.34 monthly pass through charge per household breaks down to $1.05 per wireline phone on the ILEC bill, $1.05 on each assign CMRS number, and only a three-cent a month IXC contribution per household. As with the number based-mechanism, this is a huge disparity.

IXCs still account for almost all of the interstate and international revenues, the basis of the universal service fund. Requiring ILECs to bear the vast, and extremely disproportionate burden of USF contributions while they account for only a small portion of the interstate revenues clearly violates Section 254(d) and 2(b) of the Act that require carriers to contribute on an equitable and non-discriminatory basis and prohibits an assessment on intrastate revenues to support the federal interstate universal service fund. This mechanism would give the largest generator of interstate and international revenues virtually a free ride.

### B. Proposal #2 – Connection Based Methodology

This second connection-based methodology proposal calls for an assessment on each switched access connection. Under this methodology, presubscribed switched transport providers would be assigned a connection-based assessment. Staff estimates an average monthly-pass through charge per household of $3.81, the highest of all the mechanisms evaluated and $1.33 per month higher than the estimated revenues-based pass through charge. Connection proposal #2's estimated monthly assessments per industry segment breaks down to $0.72 IXC contribution per presubscribed line, $1.45

[4] All figures used here to evaluate the mechanisms were projections for the year 2007, unless otherwise noted.

mobile wireless connection per residential handset,[5] and $0.72 assessment for each primary residential line. The study translates this into industry segment contributions of 29% on IXCs, 20% on ILECs, and 43% on CMRS providers.

This appears to be in the acceptable range to meet the equitable and non-discriminatory clause under the assumption that CMRS carrier contributions cover both the local and long-distance customer relationships. Currently, CMRS carriers are not required to provide customers with equal access to long-distance carriers, and few if any do. However, the FCC presently has before it an open proceeding on the redefinition of universal service, which includes a consideration of whether the equal access obligation, imposed on ILECs, should be extended to CMRS providers. The outcome of the redefinition proceeding could have a dramatic impact on this proposed contribution mechanism. At the very least, the FCC should provide a full evaluation of how this mechanism would be altered to comply with an equal access obligation. NTCA has consistently advocated for the extension of the equal access obligation to all carriers receiving universal service funds as a matter of competitive neutrality.

Another concern that arises through further evaluation of the second connection-based proposal is its dramatic shift in burden from multi-line businesses to residential and single-line businesses. The estimated residential/business burden ratio for the revenue-based mechanism is 42% to 58% respectively. For this connection-based mechanism estimates are 68% residential and 32% business.

Not only does this proposed mechanism favor business consumers over residential, it also appears to favor large business customers at the expense of small

[5] Assumes that wireless customer presubscribes to that wireless carrier's long-distance service. Charge is

businesses. For example, the monthly assessment for a single-line business under the revenue-based mechanism is estimated at $0.66, while for this connection-based mechanism it is estimated to more than double to $1.45. At the same time the change for the high capacity connections used primarily by big business are estimated to be reduced drastically. According to the staff study the monthly assessment for an OC3 interstate private line (priced at $17,500 per month) will decrease from $1,987.23 under the revenue-based proposal to only $486.57 under this connection-based proposal. This results in a $1,500 per OC3, per month reduction in USF assessment: A loss that appears to fall on the shoulders of residential and small single-line businesses to make up.

From its inception as internal AT&T policy, the concept of universal service was for business to offset residential rates and urban to offset rural rates. A connection to the telephone network is viewed by the FCC as a vital link to ones community and emergency services. The FCC has and continues to struggle to improve the national telephone penetration rates. By shifting such a large portion of the funding burden from business to residential consumers the agency would undermine the very foundation of universal service and may lead to some consumers disconnecting from the telephone network. Similarly, shifting a greater contribution burden from large businesses, usually located in more urban settings, to small and medium sized businesses will again disproportionately burden rural areas where the preponderance of companies are small and medium sized. This is contrary to the letter and spirit of universal service.

### C. Proposal #3 – Telephone Number Based Methodology

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double the IXC and ILEC charge.

The estimated average residential monthly pass-through charge for the telephone number based proposal is the second highest of the mechanisms evaluated at $2.86 a month, compared to $2.38 for the revenue based mechanism – a forty-eight cent a month increase. The telephone number mechanism appears to have a fair disbursement of the burden between business and residential consumers. Residential charges would fulfill 45% of the universal service funding level with the remaining 55% being met by business assessments, according to the staff survey. This compares to a 42% to 58% residential/business split for the revenue based.

However, when you look at the breakdown of the estimated monthly fee for this methodology, questions of its viability and legality surface. Specifically, the contributions by industry segments do not meet the equitable and non-discriminatory requirements of the 1996 Telecom Act. The staff study predicts the share of industry segment contributions to be 13% by IXCs, 55% for ILECs and 31% for CMRS carriers. It further estimates the monthly $2.86 charge to breakdown as $1.02 per assigned wireline number on the ILEC bill, $1.02 on each assigned CMRS number, and a fourteen-cent a month charge on IXCs per household. This is a huge disparity. IXCs still account for almost all of the interstate and international revenues, the basis of the universal service fund. Requiring ILECs to bear the vast, and extremely disproportionate, burden of USF contributions while they account for only a small portion of the interstate revenues clearly violates Section 254(d) and 2(b) of the Act that require carriers to contribute on an equitable and non-discriminatory basis and prohibits an assessment on intrastate revenues to support the federal interstate universal service fund.

This mechanism would give the largest generator of interstate and international revenues virtually a free ride. This proposal would surely face legal challenge that would result in a prolonging and escalation of the current universal service problems while a lengthy and costly legal battle ensued. In such a scenario there would be no winner.

## II. ECONOMIC ANALYSIS

Assessing universal service contributions based on retail revenues—as is currently done—is economically efficient. The goal in assessing USF contributions should be to distribute the assessments according to customer preferences, so that those elements of the PSTN that are the most heavily consumed would, in turn, result in a relatively greater contribution to the universal service fund. There is no more efficient and accurate means of measuring customer preferences than their actual expenditures on the services, as measured by retail revenues.

Consumers of telecommunications services are free to choose which services they wish to purchase, and the overall level of their expenditures. Through their expenditures, they convey very important information about how they value those services to which they have access. The most effective means of tracking this information is via the measure of retail revenues.

Retail revenues provide a clear picture of consumer preferences, as they take into account the myriad factors that go into shaping these preferences. Consumer choice in the consumption of telecommunications services is determined by the consumer's telecommunications needs, the price and availability of the service consumed, the quality and price of competing services, new technological advances, household budget constraints, the consumer's expectations for the future, etc. Retail revenues reflect, in a very direct and accurate manner, consumers' choices and preferences given all of the variables that determine these choices.

Markets are remarkably effective at collecting tremendous quantities of disparate data and instantly distilling them into their critical elements. Any similar attempt to quantify the factors noted above would be cumbersome, time consuming, expensive, and—most importantly—nowhere near as accurate.

Further, assessments based on retail revenues are self-correcting—they adjust virtually instantaneously as consumers "vote with their purse" in response to changes in technology, price, availability and price of competing services, etc. At any given point in time, the measure of retail revenues will incorporate all of the factors influencing the consumers' decisions at that very same point in time. Markets react virtually instantaneously to new information, be it in new technological developments or shifts in customer preferences.

The retail revenue method of USF assessment allows for these assessments to be levied according to customers' willingness to pay. Consequently, the assessments will be less likely to have a deleterious impact on any one or group of service providers or technologies if the methodology is non-discriminatory as it must be by law.

Other proposed methods of assessing USF contributions—the connection-based and numbers-based proposals—suffer due to their reliance on underlying artificial regulatory constructs. They must be constantly revised and updated, in order to most effectively attempt to capture the vagaries of the ever-changing market for telecommunications services. Because they are based on estimates of relationships rather than the actual relationships and lag the market rather than change dynamically, they contain an inherent error factor that can neither be accurately measured nor corrected. They are, quite simply put, inefficient when compared to the revenue based assessment method.

The diminishing revenue bas attributable to the current revenue-based mechanism are a result of regulatory arbitrage. As discussed below, the Commission should address regulatory arbitrage by expanding the universal service contribution base to include revenues of all facilities based providers. There have been huge technological advances in the last decade. The Internet has become commonplace. Consumers are replacing long-distance calls with e-mail and instant messaging. The Internet's underlying technology has led to new network protocols, such as IP telephony. Satellite and cable providers now compete against wireline incumbent carriers for voice and data traffic. Cellular providers, who sell national calling plans with bunches of free minutes, have seen their subscribership continually climb as there service quality has improved due to the migration to digital signals.

Each of these new technologies has been given some form of preferential treatment from legacy regulatory requirements that remain on wireline incumbents. For example, facilities based broadband service providers other than IXCs, LECs and CMRS carriers are not assessed. The preferences were bestowed on these new technologies in their infancy so that they could grow unfettered of legacy regulation. However, now that these technologies have begun to mature they are capturing more and more market share yet their exemptions remain. The self-correcting flexibility inherent in the revenue-based mechanism is not allowed to adjust due to the arbitrary regulatory constructs.

The result is an increase of the assessment on legacy carriers, in this case ILECs and IXCs. Data contained in the FCC's recent Industry Revenue Report noted that total toll revenues declined significantly in 2001 and is this decline is expected to continue. It also found that ILEC revenues were virtually stagnant for this same period and predicted a decline in the future. Meanwhile, the universal service fund level has climbed as the number of CETCs receiving universal service support based on the incumbents cost swell. As the assessments on legacy services increase more and more consumers will move to the new exempt technologies leading to a downward spiral in universal service support and quality of the public switched telephone network (PSTN) it supports. By eliminating the regulatory arbitrage and applying the revenue-based mechanism evenly to all interstate and international retail revenues regardless of technology used will ensure sufficient universal service funding and the long-term viability of the fund.

## III. THE COMMISSION SHOULD EXPAND THE LIST OF USF CONTRIBUTORS TO INCLUDE CABLE, WIRELESS AND SATELLITE BROADBAND INTERNET ACCESS PROVIDERS

Cable, wireless and satellite communications companies are currently using their platforms to provide broadband Internet access service in direct competition with incumbent ILEC broadband access service. None of these non-LEC broadband access providers, however, have the same universal service obligations as their ILEC competitors. Contribution policies and rules therefore should change in order to eliminate the distinct competitive advantage these companies have over contributing ILECs, as well as the drain they impose on the interstate revenue assessment base.[6]

[6] *First Repost and Order,* CC Docket 96-45, 12 FCC Rcd 9183-9184, ¶795.

Section 254(d) specifically provides the Commission with permissive authority to require "any other provider of interstate telecommunications" to contribute to universal service. Using this authority the Commission has required some entities that provide interstate telecommunications to end-users for a fee to contribute to the interstate universal service mechanisms. This category of providers includes entities that lease excess telecommunications capacity to end-users on a private contractual basis.

Under the Commission's existing contribution rules, wireline telecommunications carriers providing "telecommunications services," including broadband transmission services, are required to make USF contributions to the extent they provide broadband transmission services or other telecommunications services on a stand alone basis to affiliated or non-affiliated Internet service providers (ISPs) or end-users.[7] These rules, however, do not apply to cable, wireless, and satellite providers of broadband transmission services or broadband Internet access.[8] The Commission is tentatively proposing to redefine certain ILEC propounded broadband services as "telecommunications" and place these on a regulatory parity basis with "cable modem" services. This decision could further reduce the base of contributors. The FCC can avoid that result by assessing all broadband services.

To the extent that the Commission is concerned about competitive neutrality and the sustainability of an adequate revenue base for its interstate USF mechanisms, it should require all providers of broadband transmission or other telecommunications

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[7] *In the Matter of Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities,* CC Docket No. 02-33, *Universal Service Obligations of Broadband Providers,* and *Computer III Further Remand Proceeding: Bell Operating Company Provision of Enhances Services: 1998 Biennial Regulatory Review – Review of Computer III and ONA Safeguards and Requirements,* CC Dockets Nos. 95-20, 98-10, FCC 02-42, Notice of Proposed Rulemaking (NPRM) ¶¶ 71and 72 (rel. Feb. 15, 2002).
[8] *Id.* ¶ 79.

services on a stand alone basis to affiliated or non-affiliated ISPs or end-users to contribute on an equitable and non-discriminatory basis.[9] The Commission's rules should keep pace with competition as competitors use different facilities and technologies as substitutes for traditional circuit switched telecommunications services and broadband Internet access services. The Commission should therefore require cable, satellite, and wireless broadband Internet access providers to contribute to the federal universal service fund. Failing to position these carriers on equal footing with existing contributors will continue to place existing contributors at a distinct competitive disadvantage and further drain revenues from the existing contribution revenue assessment base.

## IV. THE STAFF STUDY SUPPORTS NTCA'S POSITION THAT THE FCC SHOULD ADOPT A "WAIT AND SEE" APPROACH

NTCA urges the Commission to take a "wait and see" approach on modifying the USF contribution mechanism. The Commission adopted interim changes to the current revenue-based system in December 2002. The Commission should allow time for its recently adopted interim changes to the revenue-based mechanism to be implemented and their impact on universal service contributions evaluated. Many of the interim changes will take effect in the second quarter of 2003. These changes will need to be factored into any staff study or analysis. Doing so may lead the Commission to determine whether further consideration of connection-based USF assessment proposals unwarranted. The new revenue-based system has increased the wireless safe harbor from 15 to 28.5 percent of wireless carrier total end-user revenues. This will add a significant infusion of revenue into the revenue-base from which the USF contribution factor is determined. This may in turn lower and stabilize the contribution factor. After

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[9] 47 U.S.C. §254(d).

monitoring the level of the contribution factor and growth of universal service support distributed to competitive eligible telecommunications carriers (CETCs), the Commission may conclude that only minor adjustments to the revenue-based system are needed to ensure the long-term sustainability and predictability of universal service support.[10]

The Commission should also refrain from further changes to the USF contribution mechanism until it has implemented its final rules in its universal service redefinition proceeding[11] and universal service portability proceeding.[12] The potential rule changes in these two proceedings will likely further assist the Commission in managing the overall size of the fund and help stabilize the contribution factor.

In addition, the Commission should use this opportunity to resolve the outstanding issue of whether to classify broadband Internet access service offered by telecommunications carriers as "telecommunications service" regulated under Title II or as "information service" regulated under Title I of the Act. Once the Commission determines the appropriate classification, NTCA urges the Commission to exercise its statutory authority to include cable, wireless and satellite broadband Internet access providers into the pool of contributors to universal service. Expanding the list of contributors is essential to the continued success of universal service and to the

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[10] Notwithstanding the Commission's final decision concerning the contribution mechanism, the Commission should continue to collect contributions for the Telecommunications Relay Service (TRS), Local Number Portability (LNP), Numbering Administration (NA), and wireline regulatory fees programs from carriers annually based on annual revenues. Paying an annual contribution is the most efficient and cost effective means to collect revenues for these support programs. Any change to the contribution process that would require monthly billing for these programs would likely result in a significant increase in carrier administrative costs. The Commission should therefore avoid imposing this additional cost burden on carriers by continuing to collect these contributions on an annual basis.

[11] *In the Matter of Federal-State Joint Board on Universal Service Seeks Comment on Review of the Definition of Universal Service,* Public Notice, CC Docket 96-45, FCC 01J-1 (rel. Aug. 21, 2001) (*Universal Service Redefinition Proceeding)*.

establishment of regulatory parity among all providers of high-speed access to the Internet.

## V. CONCLUSION

By redefining universal service, tightening the portability rules and expanding the list of contributors during its review and evaluation of the effects of its most recent changes to the revenue-based system, the Commission will slow the growth of the high-cost universal service fund, stabilize the contribution factor and may determine that further consideration of connection-based USF contribution proposals unnecessary.

As pointed out in analysis here, the two connection-based and one telephone number-based mechanisms proposed by the Commission each contain flaws. In addition, they have inherent conflicts with Section 254(d) and 2(b) of the Act that require carriers to contribute on an equitable and non-discriminatory basis and prohibits an assessment on intrastate revenues to support the federal interstate universal service fund. Nothing contained in the staff study or previous rulings has proved that a connection or number-based contribution methodology is superior to the current revenue-based mechanism. The revenue-based system has proven to work, is not administratively burdensome and has passed legal muster. With expansion of the contribution base to include all interstate revenues it can ensure the continued viability of USF. To change to an economically and

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[12] *In the Matter of the Federal-State Joint Board on Universal Service Seeks Comment on Certain Rules Relating to High-Cost Universal Service Support and the ETC Designation Process*, Public Notice, CC Docket 96-45, FCC 03J-1 (rel. Feb. 7, 2003).

administratively unproven and legally questionable methodology would not be in the public interest.

Respectfully submitted,

NATIONAL TELECOMMUNICATIONS
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April 18, 2003

CERTIFICATE OF SERVICE

I, Gail Malloy, certify that a copy of the foregoing Initial Comments of the National Telecommunications Cooperative Association in CC Docket Nos. 96-45, 98-171, 90-571, 92-237, 99-200, 95-116, 98-170, FCC 03-31 was served on this 18th day of April 2003 by first-class, U.S. Mail, postage prepaid, to the following persons.

/s/ Gail Malloy
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